

**California Debt and Investment
Advisory Commission
Fundamentals of Land Secured Financing
February 2007**

Introduction

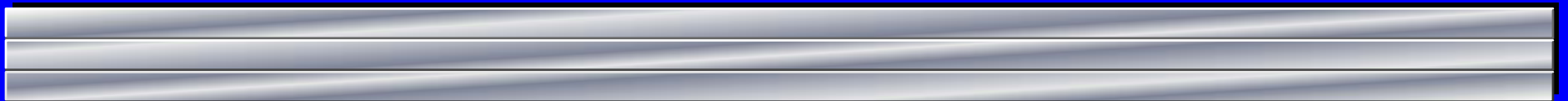
**California Debt and Investment
Advisory Commission
Fundamentals of Land Secured Financing
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Session I

*Basic Structures of Assessment
and Community Facilities
Districts*

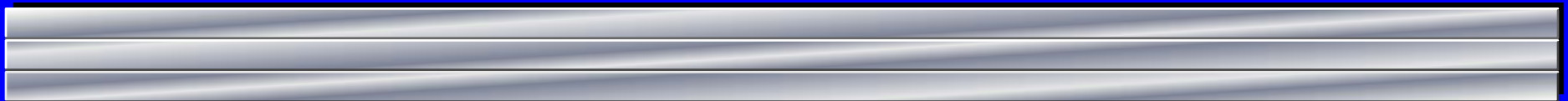
History of Each in a Nutshell

- Special Assessment Districts
 - Municipal Improvement Act of 1913
 - Used with the Improvement Bond Act of 1915
 - Other Acts normally used for maintenance
- Mello-Roos Community Facilities Districts
 - In 1978, Prop. 13 was approved by CA voters
 - In response, the Community Facilities Act of 1982 was adopted



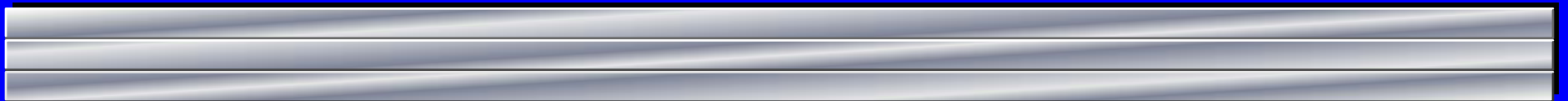
California Statutes & Constitution

- Assessment District (AD)
 - Primarily 1913 & 1915 Acts for capital projects
 - Primarily 1972 & 1982 Acts for maint./services
 - Article XIID of CA Constitution
 - Section 53753 of the Govt. Code
- Community Facilities District (CFD)
 - Mello-Roos Community Facilities Act of 1982
 - Articles XIIA & XIIC of CA Constitution
- Charter Cities can use legislative powers



Eligible Capital Facilities to Finance

- Assessment District
 - Authorized public improvements
 - Must provide local, special benefits to property
- Community Facilities District
 - Public improvements with 5+ years useful life
 - Can finance facilities:
 - Owned/controlled by issuer and/or
 - Owned, operated and maintained by other public entities
 - JCFA's with other public agencies

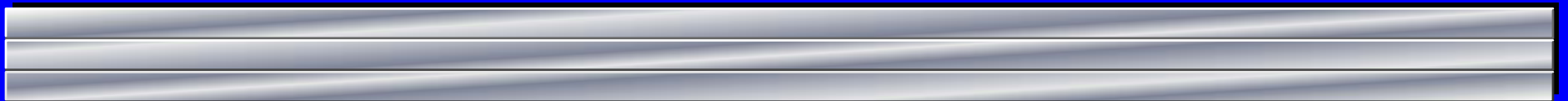


AD vs. CFD

- Assessment District
 - Sets a Fixed Lien for every parcel
 - Annual payment reduces lien
 - Term of payments = term of bonds
- Community Facilities District
 - Sets a Maximum Annual Special Tax Rate
 - Max. tax rate may escalate
 - Term of tax may outlive term of bonds
- Neither directly based on property value
 - (a.k.a. an *ad valorem* charge)

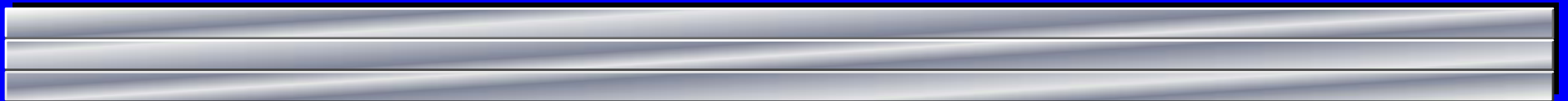
Special Benefits vs. Reasonableness

- Special Benefits - AD's
 - Assessment based on the direct and special benefit each property receives from “works of improvement”
- Reasonableness - CFD's
 - Special tax is not a special assessment
 - May be apportioned and levied on any “reasonable” basis (except ad valorem), as determined by the legislative body



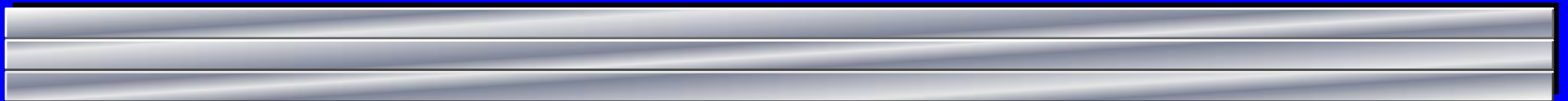
Usual Sequence of Events - AD's

1. Local agency/property owner petition initiated
2. Actions taken by Legislative Body
3. Legislative Body commences assessment proceedings
4. Public Hearing
5. Assessment balloting and “majority protest”
6. Final actions taken by Legislative Body
7. End of cash collection / statute of limitations
8. Bonds issued
9. Project costs funded / reimbursed
10. Annual assessments levied



Usual Sequence of Events - CFD's

1. Local agency/property owner petition initiated
2. Local Goals & Policies adopted
3. Legislative Body commences CFD proceedings
4. Public Hearing
5. Election
6. Final actions taken by Legislative Body
7. Bonds issued
8. Project costs funded / reimbursed
9. Annual special taxes levied



AD vs. CFD Comparison - Similarities

Issue	AD's	CFD's
Pay-as-you-go finance	1913 Act - Not common but possible 1972 Act – Permitted and fairly common	Permitted and fairly common
Pay-off or Prepayment of Lien	Automatically allowed by State statute	Allowed if included in RMA
Debt Service Structure	Almost universally level debt service	Usually level or escalating debt service
Maximum Residential Property Tax Burden as % of Sales Price	No State statutory limit. Standard is not to exceed 2%	No State statutory limit. Standard is not to exceed 2%

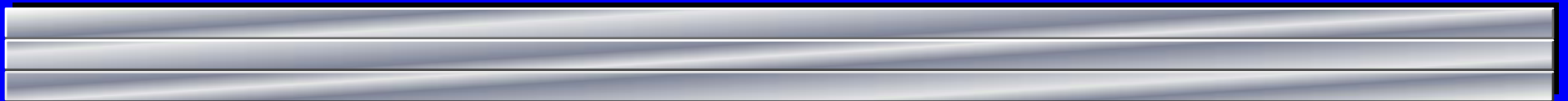


AD vs. CFD Comparison - Differences

Issue	AD's	CFD's
District Boundaries	1913 Act - Boundaries are generally fixed once assessment confirmed 1972 Act – Annexation permitted	May be expanded through future annexations
Land Use Changes	1913 Act - Lien apportionments cannot easily be modified 1972 Act – Annual assessment can adapt	Special taxes generally adapt to changes in land use
Assessment of Undeveloped Property	1913 Act - Assessments on undeveloped land is based on potential development 1972 Act – Annual assessments generally differ between undeveloped and developed parcels	Special taxes between undeveloped and developed land can differ

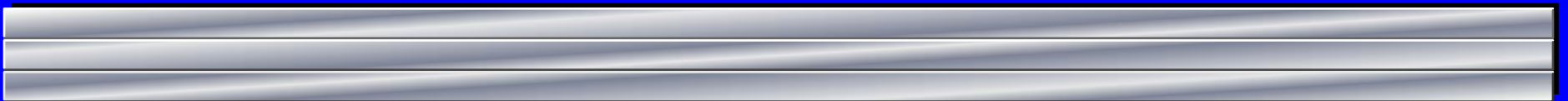
Major Factors Favoring an AD

- AD's are appropriate for:
 - Small, local infrastructure projects
 - Projects with multiple property owners
 - Large variable rate financing programs that anticipate multiple conversion of bonds to a fixed rate of interest over several years
 - Some maintenance programs and services



Major Factors Favoring a CFD

- CFD's are appropriate for:
 - General benefit “community facilities”
 - Projects with few property owners
 - Project requiring flexibility
 - Land development projects in phases
 - Uncertainties about eventual land use
 - Projects needing targeted economic burden
 - Exempting publicly-owned parcels
 - Reducing burden on select categories of parcels/uses



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Session II

Pre-Formation Considerations

Local Goals and Policies

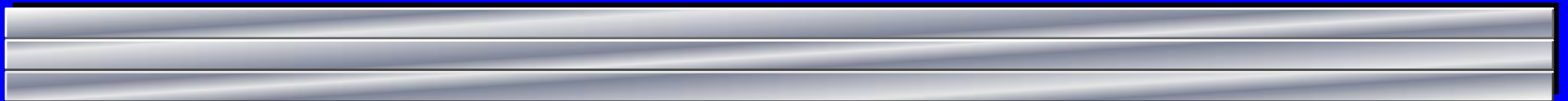
- Legal Requirement for CFD's
(Gov't code §53312.7)
- Good Idea for AD's
- Why important - to provide:
 - Guidance
 - Consistency
 - Assurances

Key Issues to Cover in Policies

- Facilities Priority & Eligibility
- Disclosure to:
 - Prospective Property Purchasers
 - Bond Buyers
 - Financial Markets
- Appraisal Criteria/Value-to-Lien
- Application Process
- Credit Quality Requirements/Criteria

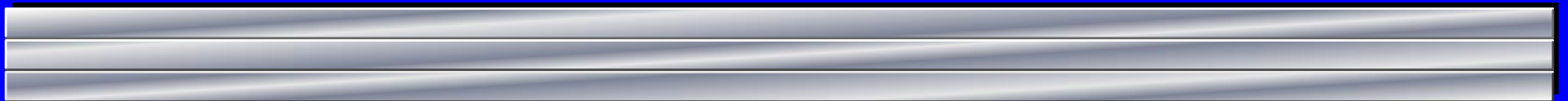
Acquisition vs. Construction

- ACQUISITION: Developer builds improvements and “sells” them
- CONSTRUCTION: Public Agency builds



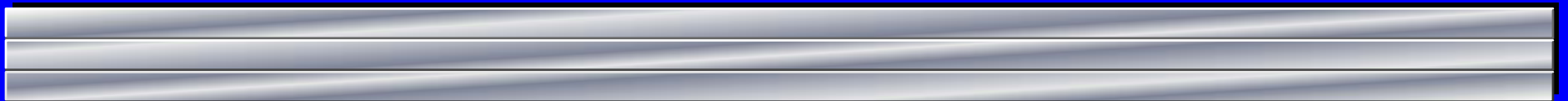
Selecting the Team

- Public Agency should choose consultants
- Financial Advisor can help
- RFP Process / Consultant Pool
- Mello-Roos / Assessment District
experience is a key



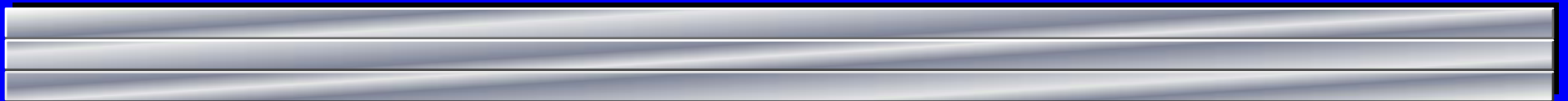
Consultant Roles

- Bond Counsel
 - Legal Opinion
- Financial Advisor
 - Guidance & market knowledge
- Special Tax Consultant
 - Tax Formula, Financing Plan &/or CFD Report
- Assessment Engineer
 - Benefit finding & Engineer's Report



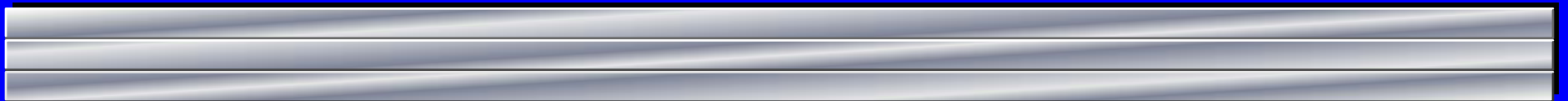
Consultant Roles (cont.)

- Market Consultant
 - Absorption Study
- Appraiser
 - Determines value of properties to be assessed / taxed



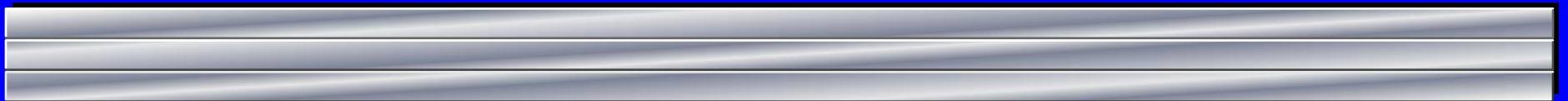
Important Considerations

- Communication among members
- Facilitation of meetings
- Involve Counsel - legal protection
- Understand structure and associated workload
(you will have to live with these decisions)



Other Agencies/Utilities Coordination

- Jurisdictional overlap
- Who will own and operate facilities?
- Joint Community Facilities Agreements required for CFD's
- Consent of legislative body required for CFD's and AD's



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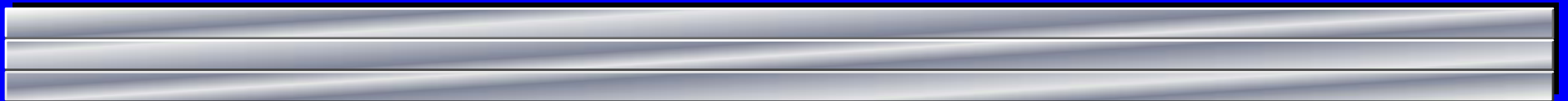
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Session III

District Formation Process

Formation Process

- LET'S GET MARRIED
 - *Petition*
- I'LL THINK ABOUT IT
 - *Resolution of Intention / Boundary Map*
 - *CFD Rate & Method of Apportionment*
 - *AD Engineer's Report (including assessment spread)*
- LET'S TALK ABOUT IT
 - *Public Hearing*
 - *AD Ballot Tabulation*
- THE WEDDING DAY
 - *Resolution of Formation*
 - *CFD Election*



Rate and Method of Apportionment

- Approved by public agency at ROF and by 2/3 vote of qualified electors
- Describes methodology used to calculate the annual special tax levy
- Must generate amount needed each year to pay bond debt service and admin expenses, to replenish reserve fund, and to pay directly for facilities and/or services.

CFD Special Tax Formulas:

Developed Property Special Tax

- Applies to parcels after issuance of building permit, recordation of map, or other defined event
- Can be spread based on benefit or market considerations, not property value
- Categories based on: land use, size of home, type of home, lot size, density, etc.
- Total tax not to exceed 2% of home's sales price
- Should be stable; no fluctuation due to additional bond sales, changes in land use, delinquencies, etc.

CFD Special Tax Formulas:

Undeveloped Property Special Tax

- Applies to parcels that do not yet meet definition of “Developed Property”
- Typically charged on a per-acre basis
- Must provide coverage under worst-case scenario prior to full development of the project
- Should absorb variability in special tax levy

CFD Special Tax Formulas: Additional Items to Consider

- Rate of Escalation (facilities vs. services)
- Order of Levy
- Backup Special Tax
- Cross-Collateralization
- Prepayment Formula

Engineer's Report

S&H Code §10204 (1913 Act)

- Plans & Specifications
- Estimate of Costs
- Assessment Diagram
- Assessment Methodology
- Assessment Roll
- Annual Administration Costs

Engineer's Report

S&H Code §2960 (1931 Debt Limitation Act)

- Total principal amount of Unpaid Assessments on parcels
- Total true value of parcels
- Total Lien / Value
(must be less than 50%, by Code)

Engineer's Report

- Key information document in a dispute
- Prepared by a Registered Prof. Engineer
- Proposition 218 requirements
 - Special Benefit should be clearly defined
 - General Benefit should be discussed
 - Assessment spread clearly detailed
 - Special treatment of public parcels should be discussed

CFD Special Election Process

- Conducted after Reso. of Formation
- This IS an election under the Elections Code
- Weighted by property area
(if fewer than 12 registered voters)
- 2/3 must vote “yes”
(registered voters or area)

Assessment Ballot Process

- Required by Proposition 218
- Mailed with Notice of Public Hearing
- This is **NOT** an election,
NOT a secret ballot
- Ballots opened and tallied after hearing
- Weighted by assessment amount
- More “no” than “yes”, no assessment

Assessment Process After Formation

- Recordation of Notice of Assessment
- 30-Day Cash Collection Period
 - Mailed Notice to Pay Assessment
 - Cash payment discount
 - Paid / Unpaid List

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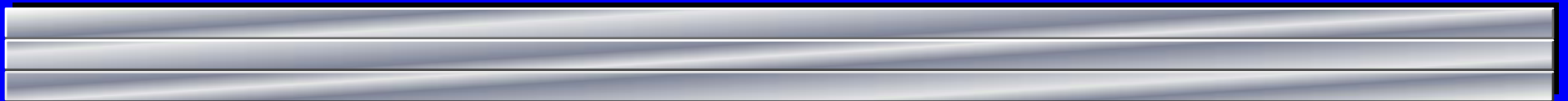
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Session IV

Project Implementation

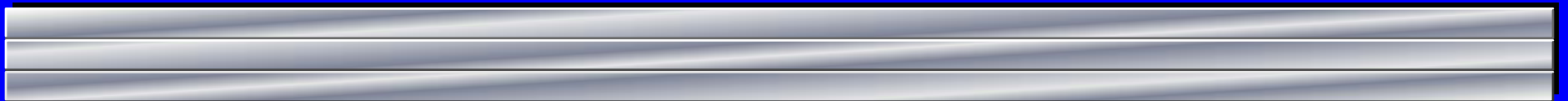
Construction or Acquisition ?

- Construction Project:
 - Issuer constructs project
 - Bond proceeds pay costs as needed
- Acquisition Project:
 - Developer/Owner constructs improvements (must front the costs)
 - Issuer to “purchase” (acquire) with bond proceeds



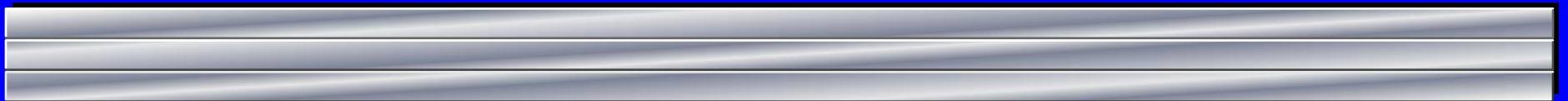
Developer Constructs Improvements

- Acquisition Agreement specifies how (construction and purchase processes)
 - Vertical vs. Horizontal
 - Completed Facility vs. Progress Payments
 - Other specifications and requirements
 - Competitive bidding
 - Prevailing wage
 - Inspection
 - Insurance
 - Local agency review of Plans & Specs



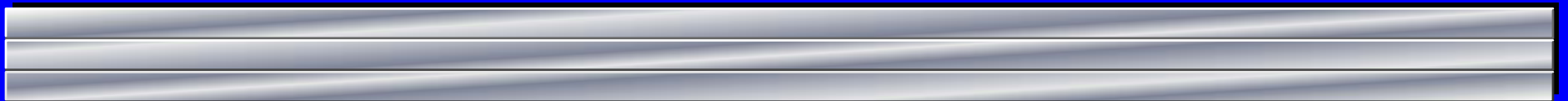
Developer Constructs Improvements

- Requirements for Developer to get paid:
 - Contracts, invoices & canceled checks
 - Evidence of transfer of title
 - Evidence of acceptance of improvements
 - Lien releases from contractor and subs
 - Amount within limits of Agreement



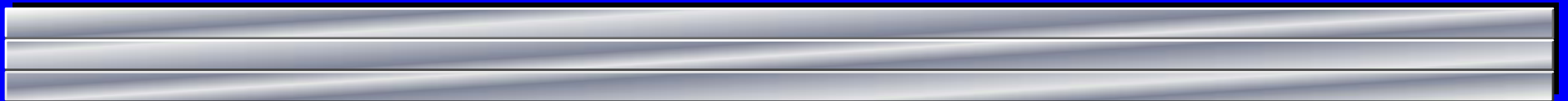
Issuer Constructs Improvements

- Expand working group to include:
 - Public Works staff
 - Representatives from other local agencies
 - Design engineer / environmental consultant
 - Contract administrator / inspectors
 - Real property appraiser



Issuer Constructs Improvements

- Project Design
- Property Acquisition
- Environmental Clearance
- Review and Approval of Plans & Specs
- Solicitation of Sealed Bids



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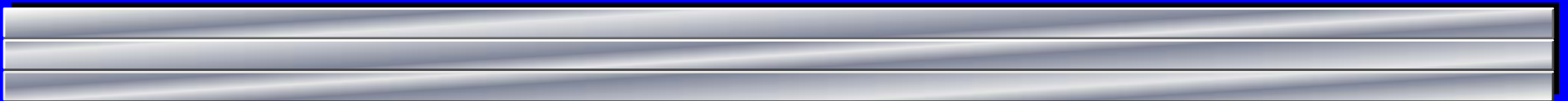
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Session V

Bond Issuance

Bond Issuance

- LET'S HAVE A BABY!
 - *Deciding to sell bonds*
- CAN WE AFFORD TO HAVE ONE?
 - *Financial Feasibility*



Bond Issuance (cont.)

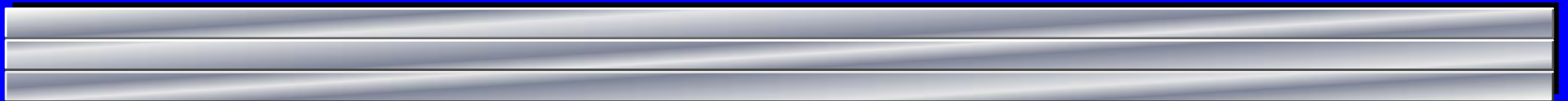
- How do we do it?
 1. Financing team drafts legal and financing documents
 2. Bond indenture
 3. Issuer approves financing documents
 4. Issuer sells bonds to underwriter
 5. Underwriter sells bonds to investors
 6. Issuer receives \$s in exchange for bonds
 7. Net proceeds used for capital projects



Expansion of Financing Team

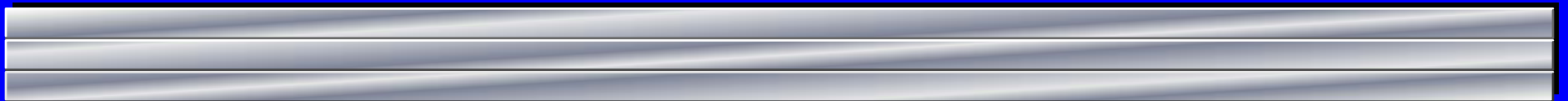
Existing Financing Team & Staff, plus...

- Appraiser
 - Estimates value of lien property
- Underwriter
 - Structures and markets the bonds
- Disclosure / Underwriter's Counsel
 - Prepares bond sale financing documents
(Official Statement, bond purchase agreement, etc.)



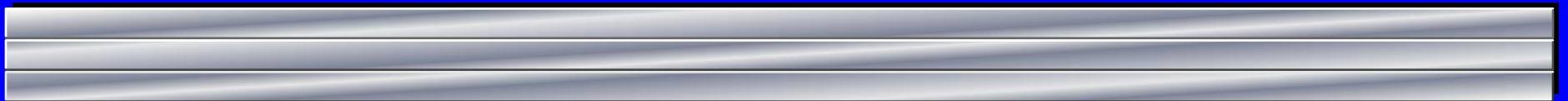
Expansion of Financing Team (cont.)

- Trustee / Fiscal Agent
 - Holds, invests and disburses funds at direction of issuer.
 - Has trust obligation to bond owners
- District Administrator
 - Assists Issuer in administering AD/CFD
(good practice to retain earlier in process)



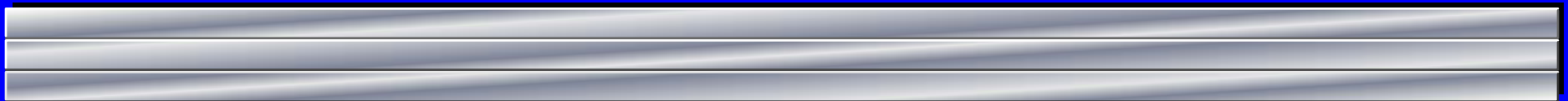
Initial Bond Disclosure

- LET'S TELL OUR FRIENDS WE'RE HAVING A BABY!
 - *Preliminary Official Statement*
 - *Tell the truth, the whole truth, and nothing but the truth*
- So what do you tell our friends?



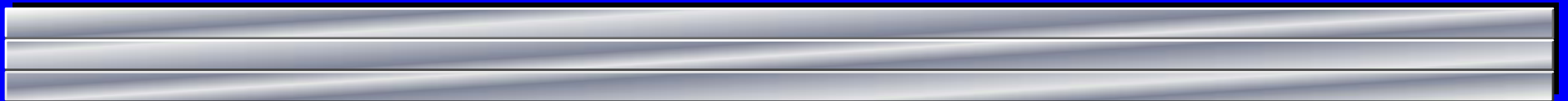
Disclosing Information to Investors

- Official Statement includes:
 - Description of the Bonds
 - Authority for issuance
 - Debt service schedule
 - Redemption provisions
 - Sources and uses, etc.
 - Project Information (what is being financed)
 - Security for the bonds
 - Special taxes / assessments
 - Land value estimates
 - Foreclosure provisions, etc.
 - Reserve fund
 - ability to issue additional debt
 - The CFD/AD Development Plan and Status
 - Project pro-forma
 - Developer information



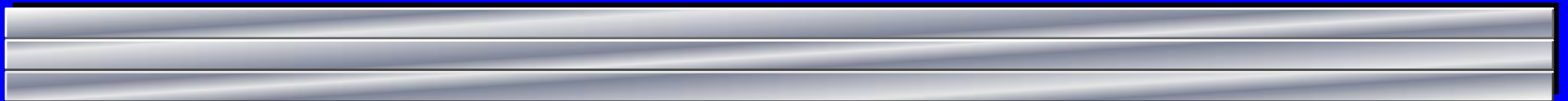
Disclosing Info to Investors (cont.)

- Official Statement also includes:
 - Bondholder Risks
 - Special Tax Formula (RMA) /
Assessment Spread (portions of Engr's Report)
 - Appraisal
 - Market Absorption Report
 - Summary of key legal documents
 - Continuing disclosure agreements



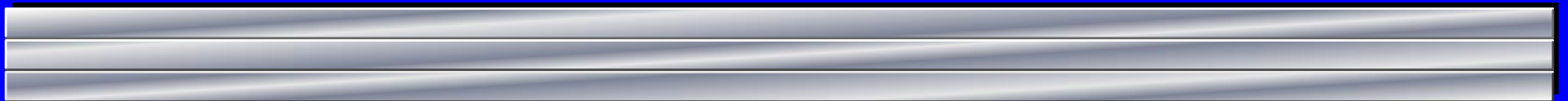
Bond Issuance Considerations

- Bond Sizing / Financial Feasibility
 - How much is needed now?
 - How much can we afford?
 - Special tax revenue coverage -
how many bonds can be supported?
- Timing of Property Tax Bill submittals relative to bond sale
 - Capitalized interest for initial period (“stub period”) or longer



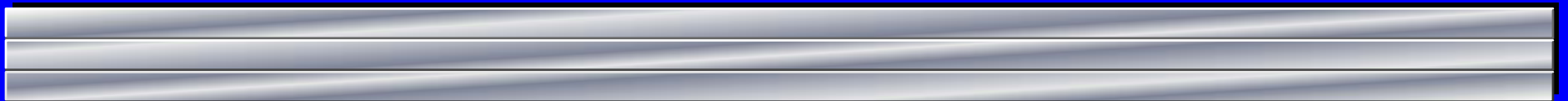
Timing of Bond Sale

- Status and progress of development
- Placing annual levy on Property Tax Bills
- Phasing of facility construction / need for funds to pay for or reimburse for facility costs
- Market Conditions



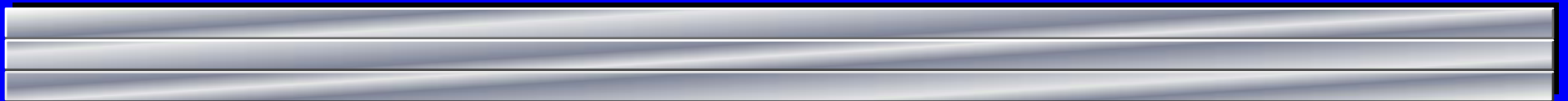
Bond Sale Overview

- Must have all required legal documents completed and approved
 - Issuer adopts all necessary resolutions
- Issuer approves Resolution of Issuance
- Issuer approves final legal documents
 - Official Statement (preliminary)
 - Continuing Disclosure Agreement(s)
 - Bond Purchase Agreement (parameters)
 - Bond Indenture or Fiscal Agent Agreement



Bond Sale Overview (cont.)

- Underwriting Firm (Investment Bank)
 - Agrees to buy all the bonds
(at a discount - wholesale)
 - Sells to individuals/institutional investors
(at retail)
- Interest rates on the bonds
 - Market's perception of credit quality of CFD/AD
 - Developer's strengths & ability to perform
 - Prevailing overall market interest rates
 - Demand for land-secured debt



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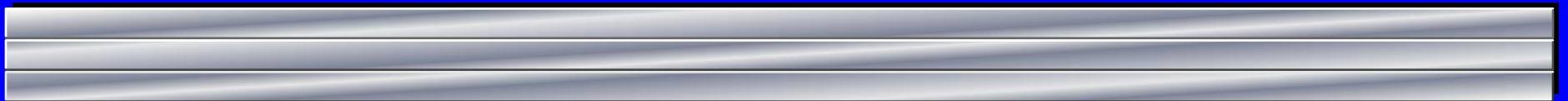
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Session VI

*Administration of Liens
and Bonds*

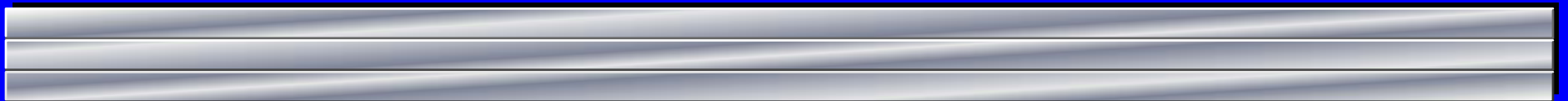
Administration - Basic Steps

- Know your CFD / AD
- Be active prior to issuance
- Manage the funds
- Meet administrative obligation
- Customer service



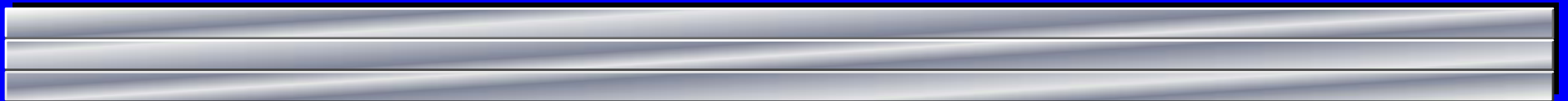
Preparing CFD / AD Levy

- Know your tax formula / assessment spread
- Update parcels & “development status”
- Allocate parcels to tax categories (CFD)
- Determine special tax requirement (CFD)
- Assessment Apportionments (AD)
- Determine debt service & admin costs (AD)
- Submit to Auditor's office



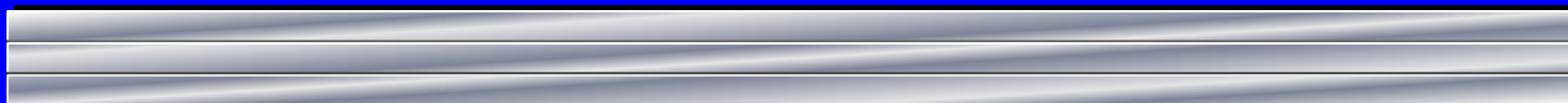
Delinquency Management

- Accelerated judicial foreclosure
- The delinquency process
 - Strip special tax / assessment levy off roll
 - Notice to delinquent owners
- Foreclosure Counsel
- Thresholds



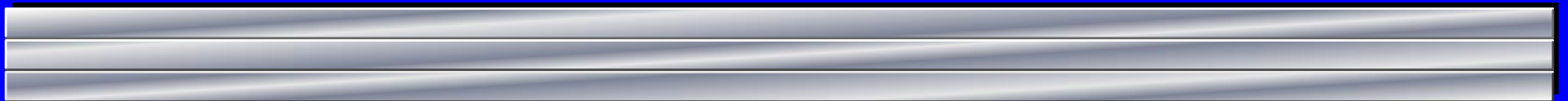
Continuing Disclosure

- SEC Rule 15c2-12
- Obligated Persons - Issuer & Developer
- What to disclose
 - Material events
 - Items in Continuing Disclosure Certificate
- Disclosure Counsel relationship
- Information Repositories - NRMSIRs
- Reports must be filed on time!



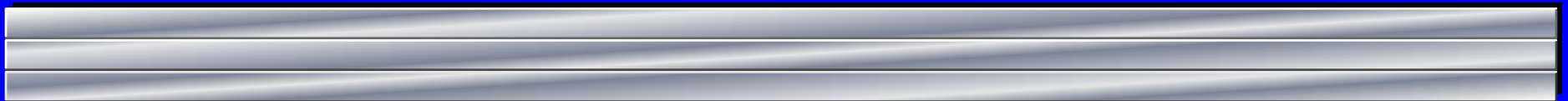
Annual Special Tax Report - CFD

- Summary of development
- Summary of account balances
- Status of improvements
- Summary of financial obligations
- List of parcels and levy
- CDIAC requirements



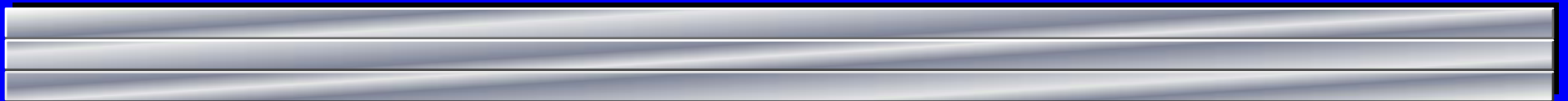
Other Administrative Items

- Arbitrage rebate calculation
- Reconcile bank statements
- Disbursing/Investing Bond Proceeds
- Prepayment calculations
- Record release of special tax / assessment lien
- Reimbursement for facility construction
- Changes of ownership in the bonds



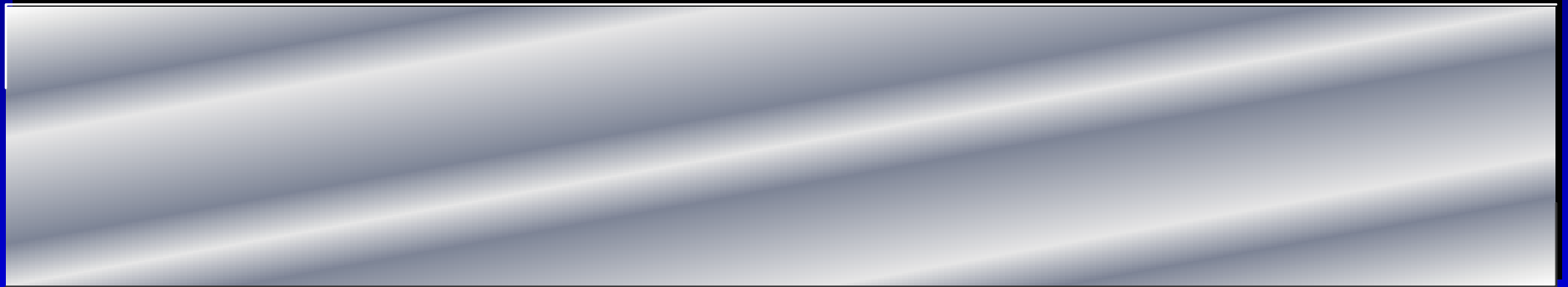
Consultants or Staff?

- Staff's experience
- Evaluation of workloads
- Number of districts
- Complexity of districts
- Combined approach



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***Workshop Conclusion
and Evaluation***